BP (BP)

Updated November 4th, 2022 by Aristofanis Papadatos

Key Metrics

Current Price:	$33	**5 Year CAGR Estimate:**	8.9%	**Market Cap:**	$101 B
Fair Value Price:	$102	**5 Year Growth Estimate:**	-16.0%	**Ex-Dividend Date:**	11/9/2022
% Fair Value:	32%	**5 Year Valuation Multiple Estimate:**	25.3%	**Dividend Payment Date:**	12/16/2022
Dividend Yield:	4.4%	**5 Year Price Target**	$43	**Years Of Dividend Growth:**	1
Dividend Risk Score:	C	**Retirement Suitability Score:**	B	**Rating:**	Hold

Overview & Current Events

BP is one of the largest oil and gas corporations in the world based on its $101 billion market cap. It is a fully integrated company and operates in two segments: upstream and downstream (mostly refining). BP has gone through extreme challenges since its major accident in 2010. It has paid about $70 billion for that accident so far. This amount is almost equal to all its earnings since. Even in 2019, nine years after the accident, BP paid $2.4 billion (24% of its earnings) for it. The company expects to pay $1.4 billion for that accident in 2022.

In early November, BP reported (1/11/22) financial results for the third quarter of fiscal 2022. The price of oil and the refining margins somewhat corrected from their extreme levels in the second quarter but European gas prices skyrocketed to an all-time high thanks to an extremely tight market. As a result, the earnings-per-share of BP slipped only -1%, from a 10-year high of $2.61 in the second quarter to $2.59, and exceeded the analysts' consensus by an eye-opening $0.64. BP has exceeded the analysts' consensus for seven consecutive quarters. It also reduced its debt for a tenth consecutive quarter and reiterated that it expects to keep raising its dividend by 4% per year if the price of oil remains around $60 or higher. In such a scenario, BP also expects to repurchase $4 billion of shares per year (~4%). Thanks to its record earnings, BP has raised its quarterly dividend by 10%. Given the exceptionally high European gas prices, we have raised our forecast for the annual earnings-per-share of BP from $6.50 to $8.50.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$5.56	$4.26	$3.96	-$1.22	$0.04	$1.03	$3.71	$2.95	-$1.69	$3.82	***$8.50***	***$3.55***
DPS	$1.98	$2.19	$2.34	$2.40	$2.40	$2.40	$2.43	$2.46	$1.89	$1.29	***$1.44***	***$1.71***
Shares[1]	3186.6	3101.9	3033.3	3068.7	3239.2	3302.9	3350.3	3392	3388	3274	***3200***	***3000***

BP has greatly improved its portfolio in recent years via the addition of low-cost reserves. Last year, BP completed its 6-year growth program, which delivered 900,000 barrels of oil equivalent per day. However, it announced a major shift in its strategy in 2020. BP will boost its investment in renewable energy sources 10-fold, and it will simultaneously reduce its investment in oil and gas projects so much that it expects to reduce its oil and gas production by -42%, from 2.6 million barrels per day now to 1.5 million barrels per day in 2030.

This historical strategic shift from its core business has greatly raised the uncertainty of future performance of BP. A shift from the core business is always a red flag for any stock, particularly for BP, which has always been infamous for its aversion of renewable energy projects. On the bright side, BP is thriving right now thanks to multi-year high oil prices. Oil producers are reluctant to boost their output amid fears over the secular shift from oil to clean energy sources but we expect them to eventually boost their output and drive oil prices lower, just like in all previous cycles. Due to the high base formed by the 10-year high earnings this year, we expect the earnings-per-share of BP to decline at a -16% average annual rate over the next five years. If the oil major achieves high returns from its renewable energy projects, it may exceed our expectations but it is in unchartered waters right now and hence it is prudent to be conservative.

[1] In millions.

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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	7.6	10.1	11.8	---	---	35.5	11.5	13.6	---	6.8	***3.9***	***12.0***
Avg. Yld.	4.7%	5.1%	5.0%	6.4%	7.3%	6.6%	5.7%	6.1%	5.2%	5.0%	***4.4%***	***4.0%***

Excluding the outlier year 2017, in which the depressed earnings resulted in an abnormally high price-to-earnings ratio, BP has traded at an average price-to-earnings ratio of 10.2 during the last decade. The stock has traded at such a cheap valuation mostly due to the excessive liabilities that resulted from its accident in 2010. We believe that a fair earnings multiple for the stock is around 12.0. BP is now trading at a price-to-earnings ratio of 3.9 due to its 10-year high earnings this year. If it trades at our assumed fair valuation in five years, it will enjoy a 25.3% annualized gain in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

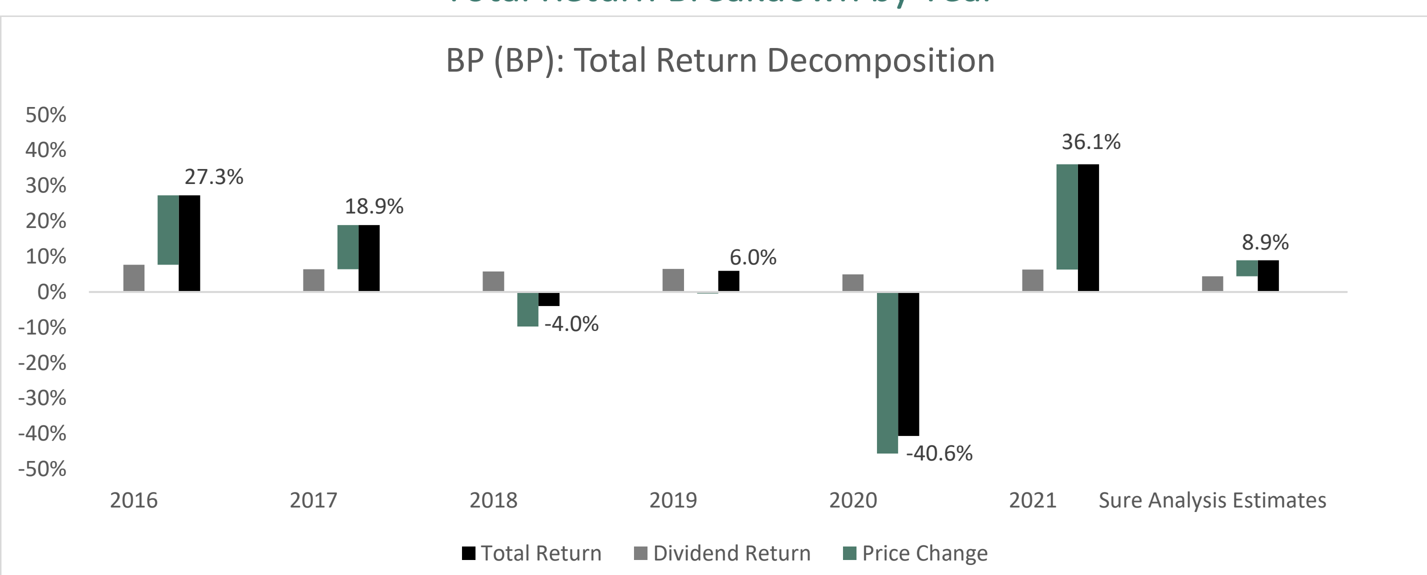
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	35.6%	51.4%	47.2%	---	---	233%	65.5%	83.4%	---	33.8%	***16.9%***	***48.1%***

After several years of a superior dividend yield, BP cut its dividend in 2020. Nevertheless, the management of BP is very shareholder friendly. Even when BP was forced to suspend its dividend after its Macondo blowout amid public outrage, it resumed its dividend payments after just three quarters. Moreover, during 2015-2017, when the company incurred material losses, it continued to pay its dividend, which amounted to about $6 billion per year. The dividend is clearly a top priority for BP's management team, but the -50% cut in 2020 was warranted due to the debt load of the company. We view the current 4.4% dividend as safe, particularly given the drastic reduction of the debt of BP in recent quarters.

Final Thoughts & Recommendation

After having incurred two fierce downturns, its accident in the Gulf of Mexico and the 2014-2017 downturn, BP faced another downturn in 2020 due to the pandemic. However, the oil major is thriving right now thanks to multi-year high oil and gas prices. BP has more than doubled off its bottom in 2020 but it remains attractive, as it could still offer an 8.9% average annual return over the next five years thanks to its 4.4% dividend and a 25.3% annualized valuation tailwind, partly offset by a -16% annual decline of earnings-per-share. The stock maintains its hold rating.

Total Return Breakdown by Year



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Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue ($B)	375.77	379.14	353.57	222.89	183.01	240.21	298.76	278.4	180.4	157.7
Gross Profit	28220	32701	26165	4809	6524	18904	28880	27,583	10,184	22,860
Gross Margin	7.5%	8.6%	7.4%	2.2%	3.6%	7.9%	9.7%	9.9%	5.6%	14.5%
SG&A Exp.	13357	13070	12266	11553	10495	10508	12179	11,057	10,397	11,931
D&A Exp.	12687	13510	15163	15219	14505	15584	16542	18,411	24,809	14,972
Operating Profit	15491	18900	13881	-6883	-4095	8288	15256	15,562	-10,493	10,505
Op. Margin	4.1%	5.0%	3.9%	-3.1%	-2.2%	3.5%	5.1%	5.6%	-5.8%	6.7%
Net Profit	11017	23451	3780	-6482	115	3389	9383	4,026	-20,305	7,565
Net Margin	2.9%	6.2%	1.1%	-2.9%	0.1%	1.4%	3.1%	1.4%	-11.3%	4.8%
Free Cash Flow	-2743	-3420	10208	485	-6010	2369	6166	10,352	-144	12,725
Income Tax	6880	6463	947	-3171	-2467	3712	7145	3,964	-4,159	6,740

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets ($B)	300.47	305.69	284.31	261.83	263.32	276.52	282.18	295.2	267.7	287.3
Cash & Equivalents	18091	20894	27499	26389	23484	25586	22468	22,472	31,111	30,681
Acc. Receivable	26485	28868	19671	13682	13393	18912	24478	24,442	17,948	27,139
Inventories	28203	29231	18373	14142	17655	19011	17988	20,880	16,873	23,711
Goodwill & Int.	13388	13355	13431	13001	12417	12880	29488	27,407	18,573	18,824
Total Liab. ($B)	180.71	175.28	171.66	163.45	166.47	176.11	180.63	194.5	182.1	196.8
Accounts Payable	29920	28926	23074	16838	21575	26983	46265	46,829	36,014	52,611
Long-Term Debt	48416	47657	52071	52465	57666	62574	65799	67,724	72,664	61,176
Total Equity ($B)	118.53	129.28	111.42	97.20	95.27	98.47	99.44	98.4	71.3	75.5
LTD/E Ratio	0.41	0.37	0.47	0.54	0.61	0.64	0.66	0.69	1.02	0.81

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	3.7%	7.7%	1.3%	-2.4%	0.0%	1.3%	3.4%	1.4%	-7.2%	2.7%
Return on Equity	9.6%	18.9%	3.1%	-6.2%	0.1%	3.5%	9.5%	4.1%	-23.9%	10.3%
ROIC	6.8%	13.5%	2.2%	-4.1%	0.1%	2.1%	5.7%	2.4%	-12.4%	4.9%
Shares Out.	3186.6	3101.9	3033.3	3068.7	3239.2	3302.9	3350.3	3392	3388	3274
Revenue/Share	117.68	119.44	114.69	72.99	58.24	72.73	89.17	81.88	53.17	46.71
FCF/Share	-0.86	-1.08	3.31	0.16	-1.91	0.72	1.84	3.04	-0.04	3.77

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.